

## Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

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Date:

November 16, 2007

## LEGEND

Distributing

StateZ

Date1

Date2

Shareholder A

a

Shareholder B

b

Shareholder C

c

Shareholder D

d

Shareholder E

e

Shareholder F

f

Family 1

Shareholder G

g

Shareholder H

h

Family 2

Business 1

Controlled

Shareholder Agreement

Dear :

This letter responds to your September 7, 2007 request for rulings regarding certain federal income tax consequences of a series of proposed transactions (collectively, the "Proposed Transaction"). The information submitted in that request and in later correspondence is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data

may be required as part of the audit process. Moreover, this office has made no determination regarding whether any distribution described below: (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations, (ii) is used principally as a device for the distribution of the earnings and profits of any distributing corporation or controlled corporation (see § 355(a)(1)(B) of the Internal Revenue Code and § 1.355-2(d)), and (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50 percent or greater interest in the distributing corporation or any controlled corporation (see § 355(e) and § 1.355-7).

### FACTS

Distributing is a StateZ corporation that was organized as a C corporation on Date1. Distributing made an S election on Date 2 (more than ten years ago).

Distributing has only one class of common stock outstanding. Shareholders A, B, C, D, E and F are members of Family 1 and together own 50 percent of the common stock of Distributing in the respective amounts of a percent, b percent, c percent, d percent, e percent, and f percent. Shareholders G and H are members of Family 2 and together own the remaining 50 percent of common stock of Distributing in the respective amounts of g percent and h percent.

Distributing is engaged in Business 1. Distributing has submitted financial information which indicates that Business 1 has had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

Controlled is a corporation that will be incorporated by Distributing as described below. For what are represented as valid business reasons, Distributing proposes the following Proposed Transaction:

:

- (i) Distributing will organize Controlled with only one class of common stock. At that time Distributing will own 100 percent of Controlled common stock.
- (ii) Distributing will then contribute 50 percent of its assets and liabilities to Controlled (Contribution) as set forth in the Shareholder Agreement.
- (iii) Immediately following the transfer of assets to Controlled, Distributing will distribute all of the Controlled common stock to the Family 1 shareholders in exchange for all of their Distributing stock (Distribution). The remaining shareholders of Distributing after the distribution will be the Family 2 shareholders.
- (iv) Immediately after its distribution to the Family 1 shareholders, Controlled will make an S election.

In connection with the Proposed Transaction, it has been represented that:

- (a) The total adjusted bases and the fair market value of the assets to be transferred to Controlled by Distributing equals or exceeds the sum of the liabilities to be actually or deemed assumed (within the meaning of § 357(d)) by Controlled plus any liabilities to which the transferred assets were subject.
- (b) The liabilities to be assumed (within the meaning of § 357(d)) by Controlled in the transaction and the liabilities to which the assets transferred from Distributing to Controlled are subject were incurred in the ordinary course of business and are associated with the assets being transferred.
- (c) No investment credit has been or will be claimed with respect to any property to be transferred between Distributing and Controlled.
- (d) Distributing neither accumulated its receivables nor made an extraordinary payment of its payables in anticipation of the transaction.
- (e) No intercorporate debt will exist between Distributing and Controlled at the time of or subsequent to the proposed distribution of Controlled stock by Distributing.
- (f) Payments made in connection with the transaction, if any, between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (g). No parties to the transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).
- (h) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee or in any capacity other than as a shareholder of Distributing.
- (i) The fair market value of Controlled's stock to be received by the shareholders will be approximately equal to the fair market value of Distributing stock surrendered by those shareholders in the exchange.
- (j) The five years of financial information submitted on behalf of Distributing is representative of Distributing's present operation, and with regard to Distributing, there have been no substantial operational changes since the date of the last financial statement submitted.
- (k) Following the transaction, Distributing and Controlled will each continue, independently and with its separate employees, the active conduct of its share of all the integrated activities of the business conducted by Distributing prior to the consummation of the transaction.

(l) The distribution of stock of Controlled is carried out for the corporate business purpose of fit and focus. The distribution of Controlled stock is motivated, in whole or substantial part, by that corporate business purpose.

(m) There is no plan or intention by its shareholders to sell, exchange, transfer by gift, or otherwise dispose of any of their stock in either Distributing or Controlled after the transaction.

(n) There is no plan or intention by either the Distributing or Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than through stock purchases meeting the requirements of Section 4.05(1) (b) of Rev Proc 96-30.

(o) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation involved in this transaction with any other corporation, or to sell or otherwise dispose of the assets of any corporation after the transaction, except in the ordinary course of business.

(p) For purposes of section 355(d), immediately after the distribution, no person (determined by applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the distribution.

(q) For purposes of section 355(d), immediately after the distribution, no person (determined by applying section 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote or 50 percent or more of the total value of shares of all classes of Controlled corporation stock that was either (i) acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the distribution or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the five year period (determined after applying section 355(d)(6)) ending on the date of the distribution.

(r) The distribution is not a part of a plan or series of related transactions (within the meaning of § 1.355-7), pursuant to which one or more persons will acquire directly or indirectly stock representing a 50-percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

(s) Distributing represents that it is an S corporation (within the meaning of § 1361(a) of the Code). Controlled will elect to be an S corporation pursuant to § 1362(a) of the Code on the first available date after the distribution and there is no plan or intent to revoke or otherwise terminate the S corporation election of either Distributing or Controlled.

(t) The transaction is not used principally as a device for the distribution of earnings and profits of Distributing or Controlled or both. See § 355(a)(1)(B).

(u) Neither Distributing nor Controlled will have accumulated earnings and profits at the beginning of their respective taxable years.

(v) Neither Distributing nor Controlled will have current accumulated earnings and profits as of the distribution date.

(w) No distribution by Distributing immediately before the transaction would require recognition of gain resulting in current earnings and profits for the taxable year of distribution.

(x) Distributing is not aware of, nor is Distributing planning or intending, any event that will result in Distributing or Controlled having positive or accumulated earnings and profits after the distribution.

Based solely on the information submitted and the representations set forth above, we rule as follows on the proposed transactions:

1. The Contribution followed by the Distribution (as described respectively in steps (ii) and (iii) above) will be a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled will each be a party to the reorganization within the meaning of § 368(b) of the Code.
2. No gain or loss will be recognized by Distributing upon its receipt of Controlled corporation stock in exchange for the transfer of assets to Controlled and the assumption of liabilities by Controlled. Sections 361(a) and 357(a) of the Code.
3. No gain or loss will be recognized by Controlled upon its receipt of assets in exchange for the issuance of shares of Controlled stock. Section 1032(a).
4. Controlled's basis in each of the assets received from Distributing will equal the basis of such asset in the hands of Distributing immediately prior to the transaction. Section 362(b).

5. The holding period for each asset received by Controlled from Distributing will include the period during which such asset was held by Distributing. Section 1223(2).
6. No gain or loss will be recognized to Distributing on the distribution of stock to the shareholders of Family 1 in the Distributions. Section 361(c)(1).
7. No gain or loss will be recognized to (and no amounts will be included in the income of) the shareholders of Family 1 upon their receipt of Controlled stock. Section 355(a)(1).
8. The basis of the Controlled stock in the hands of Family 1 shareholders will be the same as the basis of the Distributing stock surrendered in exchange therefore. Section 358(a)(1).
9. The holding period of the Controlled stock received by the Family 1 shareholders will include the holding period of the Distributing stock surrendered in exchange, provided that the Distributing stock is held as a capital asset on the day of the distribution. Section 1223(1).

#### CAVEATS

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed regarding: (i) whether the Distribution satisfies the business purpose requirement of § 1.355-2(b); (ii) whether the transaction is used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both; and (iii) whether the distribution and any acquisition or acquisitions are part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii). Further, no opinion is expressed concerning any of the Subchapter S elections.

#### PROCEDURAL STATEMENTS

This ruling letter is directed only to the taxpayers who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, any taxpayer filing its return electronically may satisfy this requirement by attaching a statement to the return that provides the date and control number of this letter ruling.

In accordance with the power of attorney on file in this office, a copy of this ruling letter will be sent to your authorized representative.

Sincerely,

***Virginia S. Voorhees***

Virginia S. Voorhees  
Senior Technical Reviewer, Branch 5  
Office of Associate Chief Counsel  
(Corporate)

cc: